

## Internal Revenue Service

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Department of the Treasury  
Washington, DC 20224

Third Party Communication: None  
Date of Communication: Not Applicable

Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:B02  
PLR-136702-08

Date:  
December 19, 2008

X =

A =

IRA =

State =

a =

D1 =

D2 =

D3 =

D4 =

Dear :

This responds to a letter dated August 21, 2008, and subsequent correspondence, submitted on behalf of X by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated in State on D1, and made an election to be treated as an S corporation effective D2. On D3, X issued a shares in the name of the trustee of A's individual retirement account, IRA. IRA is not an eligible shareholder of an S corporation under § 1361(b)(1)(B). Neither X nor X's shareholders were aware that the transfer of stock to IRA would cause X's S corporation election to terminate.

Once X learned of the termination of X's S corporation election due to the transfer of stock to an ineligible shareholder, X redeemed the shares issued to IRA on D4.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and were not motivated by tax avoidance or retroactive tax planning. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as may be required by the Secretary.

Section 1361(a)(1) of the Code provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1)(B) provides that the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Rev. Rul. 92-73, 1992-2 C.B. 224, provides that a trust that qualifies as an IRA under § 408(a) is not a permitted shareholder of an S corporation under § 1361. In addition, Rev. Rul. 92-73 notes that, when an S corporation inadvertently terminates due to the transfer of S corporation stock to an IRA, relief may be requested pursuant to § 1362(f).

Section 1362(d)(2) provides that (A) in general, an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation and (B) any termination under § 1362(d)(2) shall be effective on and after the date of cessation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in the ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken (A) so that the corporation is a small business corporation or (B) to acquire the shareholder consents; and (4) the corporation and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in the ineffectiveness or

termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

Based solely on the representations made and the information submitted, we conclude that X's S corporation election terminated on D3, under § 1362(d)(2), because of the transfer of shares of X to an ineligible shareholder, and that this termination of X's S election was an inadvertent termination within the meaning of § 1362(f). Accordingly, pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from D3 and thereafter, provided X's S corporation election was valid and was not otherwise terminated under § 1362(d).

As a condition for this ruling, for the tax periods from D3 to D4, in which X reported a net loss, IRA will be treated as the shareholder of the shares of stock. Otherwise, A must be treated as the shareholder of the a shares of stock for the tax periods from D3 to D4. Accordingly, all of X's shareholders, in determining their respective income tax liabilities during the termination period and thereafter, must include their pro rata share of the separately stated items of income (including tax-exempt income), loss, deduction, or credit and non-separately stated computed items of income or loss of X as provided in § 1366, make any adjustments to basis provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat X as described above, including filing any necessary amended income tax returns within 60 days of the date of this letter, this ruling will be null and void. A copy of this letter should be attached to any such returns.

Except as specifically ruled above, we express no opinion concerning the federal tax consequences of the transactions described above under any other provisions of the Code. In particular, we express no opinion on whether X is otherwise eligible to be an S corporation.

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file, a copy of this letter is being sent to X's authorized representative.

Sincerely,

Bradford R. Poston  
Senior Counsel, Branch 2  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures: 2  
Copy of this letter  
Copy for § 6110 purposes